

# PHILIPPINES ECONOMIC WRAP-UP

## APRIL 7-20, 2001

### ----- Summary -----

After a hiatus last week in light of Philippine Holy Week holidays, the 'Wrap-Up' resumes with our regular reports on Philippine forex, debt and equity markets. The Philippine central bank took another major step in improving banking system stability with the issuance of new capital adequacy guidelines patterned after the Basle Framework. Also on banking, we note the launching of a new liquidity fund for the Real Time Gross Settlement system and the latest moves in the effort to rehabilitate Urban Bank. The Social Security System has predicted that without major increases in contribution rates it will go broke. And Philippine imports continue to drop, suggesting that despite expressions of optimism, the real economic recovery has yet to begin.

These weekly reviews are available on the Embassy's web site (<http://usembassy.state.gov/manila>). We provide a longer and more detailed review of the Philippine economy in our February 2001 Economic Outlook, which is now available on our web site. The next edition of the Outlook will be released in early June.

### ----- Contents -----

#### MARKET AND POLICY DEVELOPMENTS

- Forex Report
- Credit Market Report
- Stock Market Report
- BSP Issues New Capital Adequacy Guidelines
- Banking Notes
  - Liquidity System For RTGS
  - Lone Taker For Urban Bank
- Jan-Feb Imports Drop 9.1% Year-On-Year
- Social Security System Funds Drying Up

-----

## Market and Policy Developments

-----

### FOREX REPORT

-----

The Philippine peso continued to fluctuate in a relatively narrow band around P50/US\$ in the past two weeks. Trading was very light amidst the Holy Week break, and driven mostly by liquidity needs. As volume returned during the week of the 16th, interest rate movements and regional currencies influenced much of the activity. From a close of P50.20/US\$ on April 6, the peso moved only slightly until it closed at P50.28/US\$ on April 20.

-----

### Exchange Rate Tables

-----

Date	Weighted Average (Pesos/US\$)	Closing (Pesos/US\$)	Volume (Million US\$)
	-----	-----	-----
MAR 12	48.177	48.145	138.8
13	48.159	48.160	130.8
14	48.141	48.200	66.0
15	48.367	48.430	148.5
16	48.627	48.500	149.2
 MAR 19	 48.551	 48.505	 128.5
20	48.496	48.440	131.7
21	48.580	48.633	150.1
22	48.797	48.955	159.5
23	49.048	49.135	138.0
 MAR 26	 49.221	 49.185	 64.8
27	49.120	49.165	87.0
28	49.208	49.215	107.5
29	49.378	49.355	157.1
30	49.371	49.510	122.4
 APR 02	 49.717	 49.770	 104.0
03	49.743	49.730	140.0
04	49.880	50.160	137.9
05	50.182	50.175	139.9
06	50.372	50.200	160.6

APR 09	Markets Closed		
10	50.017	49.900	78.5
11	49.880	49.930	69.5
12	Markets Closed		
13	Markets Closed		
APR 16	50.086	50.200	99.3
17	50.238	50.300	105.3
18	50.173	50.110	162.0
19	50.054	50.060	136.5
20	50.218	50.280	141.1

-----  
Source: Bankers Association of the Philippines

#### **CREDIT MARKET REPORT**

-----

With National Treasurer Sergio Edeza saying that bids were 'unreasonable', the Treasury Bureau rejected some P5.3 billion worth of offers to buy T-bills at the regular April 16 auction, awarding only P1 billion worth of 91-day bills. (The Treasury regularly offers P4 billion worth of T bills for auction each Monday: P 1 billion worth of 91-day bills and P1.5 billion each of 182-day and 364-day bills.) As a result, the average interest rate for the 91-day bills rose to 10.027, a 6.8 basis point increase from the April 10 auction. Rates on the longer term bills could have risen as much as 43 basis points were all bids accepted. Traders cited a depreciating peso and increased government demands for local funds to finance budget deficit projections as reasons for the move to push rates higher.

But the surprise move of the U.S. Federal Reserve to cut its overnight rates by 50 basis points encouraged the policy-making Monetary Board of the Bangko Sentral ng Pilipinas (BSP, the central bank) to follow suit. On April 19, the BSP cut overnight borrowing and lending rates to 9.5% and 11.75%, respectively. In making the announcement, BSP Governor Rafael Buenaventura told reporters that the rate cut was predicated on moderate inflation and marginally improved domestic demand. The US cut offered the BSP more 'flexibility.' The BSP hopes

that the rate cut will further reduce the incentive for commercial banks to park funds with the BSP and to use them instead for commercial lending activities; lower rates should also help to boost weak loan demand. Several bank treasury officers, however, suggest they will wait to see how T-bill rates respond next Monday before moving to reduce their lending rates.

-----  
Domestic Interest Rates (in percent)  
-----

Treasury Bills  
-----

Auction Date	91 days	182 days	364 days
-----	-----	-----	-----
MAR 12	9.893	10.983	11.788
MAR 19	9.656	10.356	11.340
MAR 26	9.059	10.331	10.957
APR 02	9.611	10.479	11.026
APR 10	9.959	11.005	11.638
APR 16	10.027	no sales	no sales

Source: Bureau of the Treasury

Prime Lending Rates of 14 Expanded Commercial Banks  
-----

Date of Survey	Average	Range
-----	-----	-----
MAR 08	14.3913	12.00 - 19.00
MAR 15	13.6914	11.50 - 15.25
MAR 22	13.5156	11.25 - 14.656
MAR 28	13.0484	10.75 - 14.50
APR 05	13.1808	10.75 - 14.611
APR 19	13.4611	11.00 - 15.027

Sources: Bangko Sentral ng Pilipinas; Press reports

**STOCK MARKET REPORT**  
-----

After sinking to levels last seen just before the ouster of former President Estrada in January, the Philippine Stock Exchange broadly shrugged off the unexpected interest rate cut on April 19. Investors continue to be

concerned about weak corporate earnings data as well as continuing volatility in equity markets regionally and world-wide. From its April 6 close of 1471.13, the 33-share Philippine Stock Index (PHISIX) fell to close at 1428.54 on April 20. Its lowest close to date in 2001 came on April 19 when the PHISIX sank to 1425.97. The PHISIX stood at 1438.21 on January 18, 2 days before the removal of former President Estrada.

-----  
Philippine Stock Exchange Index (PHISIX) and  
Value of Shares Traded  
-----

Date	PHISIX Close	Value (Million pesos)
----	-----	-----
MAR 12	1567.53	196
13	1526.40	348
14	1523.79	266
15	1491.79	383
16	1498.32	309
 MAR 19	 1507.52	 374
20	1491.54	335
21	1471.56	277
22	1466.23	420
23	1431.57	486
 MAR 26	 1448.37	 586
27	1446.99	401
28	1451.55	475
29	1430.16	346
30	1446.40	438
 APR 02	 1439.05	 326
03	1452.26	292
04	1452.15	317
05	1460.67	588
06	1471.13	713
 APR 09	 Markets Closed	
10	1459.49	479
11	1445.26	445
12	Markets Closed	
13	Markets Closed	

APR 16	1453.84	236
17	1435.68	271
18	1425.97	507
19	1428.87	614
20	1428.54	411

-----  
Source: Philippine Stock Exchange

#### **BSP ISSUES NEW CAPITAL ADEQUACY GUIDELINES**

-----

The BSP recently released new guidelines (BSP Circular 280) requiring banks to adopt, by July 1, a risk-based capital adequacy ratio patterned after the Basle framework (with some adaptations suited to local conditions and practices). Before passage of the General Banking Law (GBL) of 2000, legal obstacles had prevented the Bangko Sentral from moving towards the Basle framework. BSP officials hailed the impending change as an important step towards aligning Philippine prudential requirements with international best practice in a rapidly globalizing world economy. BSP officials noted that the newly issued guidelines initially cover capital requirements for credit risks, pending issuance of supplementary guidelines covering market risks.

Among other changes, the new framework introduces "Tier 2" capital (which includes, subject to certain limitations and conditions, general loan loss provisions and subordinated debt instruments) in the computation of a bank's capital to risk assets ratio. Under BSP Circular 280, "Tier 2" capital should not exceed 50% of "Tier 1" (i.e., core/equity) capital. The circular also deducts intangible items -- such as "goodwill" -- from the determination of Tier 1 capital. On the assets side, the new framework considers both on-balance and off-balance sheet items, as well as adopts a more refined risk weighting system (0%, 20%, 50% or 100% -- from 0% and 100% currently) depending on the type of assets and exposure.

The minimum capital adequacy ratio under the risk-weighted framework will be maintained at the current 10%

(higher than the internationally-accepted 8% standard). For greater transparency and more effective monitoring, the 10% ratio should be maintained on a solo basis (head office plus bank branches) as well as on a consolidated basis (bank plus financial allied subsidiaries). BSP officials told the Embassy that their internal "test run" indicated that most banks would be able to comply with -- if not better -- the 10% minimum capital to risk-weighted ratio computed according to the new framework.

## **BANKING NOTES**

-----

**Liquidity Facility for RTGS:** At the end of March, the Bangko Sentral launched the initial phase of a Real Time Gross Settlement System (RTGS). The RTGS is currently limited to interbank call and term loans and government securities under repurchase agreements with the BSP -- transactions which, under RTGS, are now settled on a gross, trade-by-trade basis (BSP Circular 266). The RTGS is being implemented through an upgraded, electronic Multi-transaction Interbank Payment System (MIPS2).

The BSP's Monetary Board also approved the establishment of an Intra-day Liquidity Facility (ILF) to support the implementation of BSP Circular 266. The ILF is intended to prevent the possibility of failed settlements through MIPS2 for interbank transactions not covered by Circular 266 and which are still being settled on a net (versus gross, trade-by-trade) basis. These interbank transactions include primary auctions and secondary trading of government securities; peso netting for \$-peso swaps; and lending activities including collections and repayment. The ILF -- considered part of the BSP's open market operations -- basically operates like a repurchase arrangement backed up by eligible, peso-denominated securities issued by the national government.

**Lone Taker for Urban Bank:** Only one party tendered a rehabilitation proposal for closed Urban Bank and its investment house subsidiary on the April 16 deadline set by the Philippine Deposit Insurance Corporation (PDIC). A group representing Urban Bank's smaller depositors and creditors (the National Association of Urban Bank Depositors and Creditors, NAUD) tied up with Export and Industry Bank (Exportbank, ranked 39th by assets out of

the 45 commercial banks operating in the country). The rehabilitation proposal reportedly involves converting at least 10% of deposits and placements in Urban Bank and its investment house into equity; Exportbank infusing P300 million in fresh capital; initially reopening the bank as a thrift (versus commercial) bank; and eventually merging Urban Bank and Exportbank. The group reportedly plans to "invite" Urban Bank's largest depositors -- i.e., Meralco, Petron and San Miguel Corp. (which have combined deposits estimated at P2.5 billion) -- to join the partnership. These companies had agreed to convert P750 million in deposits to equity under the rehabilitation plan spearheaded but eventually abandoned by the Bank of Commerce.

At least five local banks earlier reported to be interested in Urban Bank decided to stay away. Various press reports quoted industry sources as saying that interested bidders, like the Bank of Commerce, were spooked by legal questions surrounding the bank's closure. The PDIC, which will evaluate the NAUD/Exportbank proposal with the help of its financial adviser, expects to make an announcement on or before April 26 (the first anniversary of Urban Bank's closure).

#### **JAN-FEB 2001 IMPORTS DROP 9.1% YEAR-ON YEAR**

-----

The Philippines' import bill declined by 11.7% year-on-year in February, after declining 6.8% in January. Cumulative two-month imports fell by 9.1% from 2000's comparable level. Because of the import drop, the two-month merchandise trade surplus more than doubled to \$1 billion year-on-year despite lethargic export growth (which expanded by only 1.3%). Weak imports partly reflect weak export revenues from shipments of electronic products. Electronics exports (which comprise about 60% of export receipts and rely heavily on imported inputs) are being hit by a "double whammy" -- i.e., cyclical inventory adjustments and slowed demand from major markets. From a broader perspective, the lethargic trade numbers also may indicate a first-quarter slowdown in domestic economic activity; and, despite various expressions of improved optimism and confidence in the

new Macapagal-Arroyo administration, still-cautious investment and inventory policies.

-----  
PHILIPPINE FOREIGN TRADE PERFORMANCE  
(FOB Value in Million US\$)  
-----

	Exports	Imports	BOT
	-----	-----	---
Jan 2000	2,717	2,651	65
Feb	2,902	2,483	419
Jan-Feb 2000	5,619	5,134	485
Jan 2001	2,889	2,472	417
Feb	2,805	2,193	612
Jan-Feb 2001	5,694	4,665	1,029

-----  
Source: National Statistics Office

**SOCIAL SECURITY SYSTEM FUNDS DRYING UP**  
-----

Actuarial computations by the Social Security System (SSS) indicate that the private sector pension fund could run dry in fourteen years. SSS officials told the Embassy that pension benefits have been increased across-the-board ten times over the past decade and other benefits upgraded; however, employers, workers and even government repeatedly rejected increases in contribution rates. These increases have combined with changing demographics (i.e., more pensioners and fewer contributors than earlier anticipated) to exert pressure on SSS' finances. Over the past decade, the average annual growth of member benefits (17.9%) outpaced that of contributions (16.1%) and operating expenses (20.9%). In five of those years, the level of benefits exceeded member contributions. The ratio of fund assets to benefits declined from 7.1 to 4.3 between 1991 and 2000.

More recently, the pension fund reportedly lost a significant sum from its growing portfolio of stock market investments, aggravating the situation. SSS net revenue plunged to P3.5 billion in 2000 compared to an average level of 12.9 billion from 1996-1999. (Comment: The two former heads of the SSS and Government Service

Insurance System have testified that the former Philippine president and his cronies also had allegedly used the pension funds in stock market deals for private gain. End Comment.)

SSS officials estimated that doubling the contribution rate (currently 8.4% of monthly salaries) would add some 20 years to the fund's life. A specific rate has yet to be announced but SSS officials indicated that the adjustment would be staggered, with the first one planned within the year. The Government Service Insurance System imposes a higher contribution rate and is in better financial shape. GSIS officials estimated that the government employees' retirement fund had enough resources to cover claims until 2036.